PLEASE NOTE

This copy of the Interim Rule titled "National School Lunch Program: School Food Service Account Revenue Amendments Related to the Healthy, Hunger-Free Kids Act of 2010"has been submitted to the Office of the Federal Register for publication on June 13, 2011. As this rule has not yet been reviewed by the Office of the Federal Register for publication, there may be some editorial differences between this version of the Interim Rule and the final version that will appear in the Federal Register.

FNS is making available this copy of the Interim Rule for public viewing on this site prior to publication in the Federal Register in order to provide the public an early opportunity to view this rulemaking and prepare for the statutory July 1 implementation date. Although FNS does not anticipate substantive revisions to this Interim Rule, the information in this rule is not intended to and does not commit FNS to specific conclusions or actions. Once published in the Federal Register, this Interim Rule will also be available for public viewing and comment on Regulations.gov.

Billing Code: 3410-30-P

DEPARTMENT OF AGRICULTURE

Food and Nutrition Service

7 CFR Part 210

RIN 0584-AE11

National School Lunch Program: School Food Service Account Revenue Amendments Related to the Healthy, Hunger-Free Kids Act of 2010

AGENCY: Food and Nutrition Service, USDA

ACTION: Interim rule.

SUMMARY: This rule amends National School Lunch Program (NSLP) regulations to conform to requirements contained in the Healthy, Hunger-Free Kids Act of 2010 (Public Law 111-296) regarding equity in school lunch pricing and revenue from nonprogram foods sold in schools. This rule requires school food authorities (SFAs) participating in the NSLP to provide the same level of financial support for lunches served to students who are not eligible for free or reduced price lunches as is provided for lunches served to students eligible for free lunches. This rule also requires that all food sold in a school and purchased with funds from the nonprofit school food service account, other than meals and supplements reimbursed by the Department of Agriculture, must generate revenue at least equal to the cost of such foods.

DATES: **Effective date**: This rule is effective on July 1, 2011.

Comment dates: Comments on rule provisions: Mailed comments on the provisions in this rule must be postmarked on or before (insert date 90 days after publication in the Federal Register); e-mailed or faxed comments must be submitted by 11:59 p.m. on (insert date 90 days after

publication in the Federal Register); and hand-delivered comments must be received by 5:00 p.m. (insert date 90 days after publication in the Federal Register) to be assured of consideration.

Comments on Paperwork Reduction Act requirements: Comments on the information collection requirements associated with this rule must be received by (insert date 60 days after publication in the Federal Register).

ADDRESSES: The Food and Nutrition Service (FNS) invites interested persons to submit comments on this interim rule. Comments may be submitted by any of the following methods:

- Federal eRulemaking Portal: Go to http://www.regulations.gov. Follow the online instructions for submitting comments.
- Fax: (703) 305-2879, attention Julie Brewer.
- Mail: Julie Brewer, Chief, Policy and Program Development Branch, Child Nutrition Division, Food and Nutrition Service, Department of Agriculture, 3101 Park Center Drive, Room 640, Alexandria, Virginia 22302-1594.
- Hand Delivery or Courier: Deliver comments to 3101 Park Center Drive, Room 640, Alexandria, Virginia 22302-1594, during normal business hours of 8:30 a.m.-5:00 p.m.

All submissions received in response to this interim rule will be included in the record and will be available to the public. Please be advised that the substance of the comments and the identity of the individuals or entities submitting comments will be subject to public disclosure. FNS may also make the comments publicly available by posting a copy of all comments on http://www.regulations.gov.

FOR FURTHER INFORMATION CONTACT: Julie Brewer, Chief, Policy and Program Development Branch, Child Nutrition Division, Food and Nutrition Service, 3101 Park Center Drive, Alexandria, Virginia 22302, or by telephone at (703) 305-2590.

SUPPLEMENTARY INFORMATION:

I. Discussion of Interim Rule

This interim rule promulgates the provisions from sections 205 and 206 of Public Law 111-296, the Healthy, Hunger-Free Kids Act of 2010 (the Act). Section 205 amended section 12 of the Richard B. Russell National School Lunch Act (NSLA) (42 U.S.C. 1760) by adding a new subsection (p), "Price for a Paid Lunch" which addresses, for the first time, requirements for SFAs in establishing prices for paid reimbursable lunches (hereinafter called paid lunches). The amendments made by Section 205 provide SFAs with some flexibility in phasing-in any increases in paid lunch prices and in using non-Federal funds to supplement paid lunch revenue to enable them to maintain lower prices for paid lunches. There is also a requirement in section 205 requiring the Department of Agriculture (USDA) to establish procedures to annually collect and publish the paid lunch prices charged by SFAs. These provisions do not apply to the revenue from or prices charged for either afterschool snacks or for school breakfasts offered in 7 CFR part 220.

Section 206 of Public Law 111-296 amended section 12 of the NSLA by adding a paragraph (q), "Nonprogram Food Sales." This provision addresses food sold in schools outside of reimbursable meals and meal supplements, which is purchased with funds from the nonprofit school food service account. Included are foods sold in competition with the reimbursable meal programs as provided in section 10 of the Child Nutrition Act (42 U.S.C. 1779). The law now

requires that the proportion of total school food service revenue provided by the sale of nonprogram foods to the total revenue of the school food service account be equal to or greater than the proportion of total food costs associated with obtaining nonprogram foods to the total costs associated with obtaining program and nonprogram foods from the account.

FNS currently has no regulatory requirements regarding pricing of paid lunches, the amount of revenue generated by paid lunches or on the revenue generated by selling nonprogram foods. Following is a discussion of the Act's provisions and the conforming regulatory amendments being made in response. In addition to this interim rule, USDA will issue guidance and provide technical assistance as needed to assist SFAs and State agencies in complying with these new provisions.

Reimbursement Levels

There are three levels of Federal cash reimbursement for lunches, breakfasts, and meal supplements served to children in schools that participate in the NSLP and the School Breakfast Program (SBP). Schools receive the highest amount of reimbursement for meals served to students certified eligible for free meals, a lesser amount of reimbursement for students certified eligible for reduced price meals, and the lowest reimbursement for meals served to students who are not certified eligible for free or reduced price meals (i.e., paid meals).

Children in families with income at or below 130 percent of the income poverty guidelines prescribed by the U.S. Department of Health and Human Services are eligible for free meals. In addition, children who are categorically eligible because they receive other assistance (for example, receipt of Supplemental Nutrition Assistance Program benefits or enrollment in Head Start) are eligible for free meals. Children in families with income between 130 and 185 percent

of the income poverty guidelines are eligible for reduced price meals. The maximum charge for a reduced price lunch is established in section 9(b)(9) of the NSLA and cannot exceed 40 cents. A maximum reduced price charge is also established for afterschool snacks and school breakfasts. Any child not certified for a free or reduced price meal must pay the meal price set by the school food authority.

Revenue from Paid Lunches

The Act defines the term paid lunch as a reimbursable lunch served to students who are not certified to receive free or reduced price meals. NSLP regulations at 7 CFR 210.2 are amended to incorporate this definition.

The Act requires SFAs to evaluate the prices they charge for paid lunches in relation to the Federal paid and free reimbursement rates. For each school year, beginning July 1, 2011, SFAs must annually establish paid meal prices in accordance with the procedures in the Act. Those procedures are contained in a new paragraph (e) added to §210.14. In addition, §210.19(a)(2) is amended to require each State agency administering the NSLP to ensure that SFAs comply with the procedures. FNS developed a fact sheet to help schools understand the procedures. The Equity in School Lunch Pricing Fact Sheet can be found at www.fns.usda.gov/cnd/Governance/Legislation/Pricing_Equity_Facts.pdf. A summary of the procedures follows.

The Act requires SFAs to determine the average price charged for paid lunches in the previous school year (for the school year beginning July 1, 2011, the previous school year is the school year beginning July 1, 2010). The school food authority must determine the average price charged based on the total number of paid lunches claimed at each price in the school food

authority for the month of October of the prior school year. October data is used because it conforms to current data collection practices in the NSLP and is representative of the number of days of operation and number of meals served. Choosing a later month in the school year could unnecessarily delay pricing decisions by SFAs.

Calculating the average lunch price based on the number of meals claimed at each price across the school food authority most accurately indicates the revenue generated from paid lunches, which is the intent of Section 205. Requirements for determining the average paid lunch price are in §210.14(e).

Once this average is determined, the school food authority must calculate the difference between the free lunch per meal reimbursement rate and the paid lunch per meal reimbursement rate in effect for the previous school year (the "reimbursement difference"). The lunch reimbursement rates used in this calculation must be those received by the school food authority (e.g., taking into account locality (contiguous United States, Alaska or Hawaii) and additional Federal per meal reimbursement when 60 percent of lunches served in the second preceding year were served free or reduced price).

If a school food authority's average price of a paid lunch is equal to or greater than the reimbursement difference, the school food authority is not required to make any adjustments in lunch prices or to add revenue as long as it continues to charge an average price that is not less than the amount of the reimbursement difference. Further, the school food authority has the option to round the average price down to the nearest five cents. A school food authority may reduce its average price of a paid lunch if an equivalent amount of financial support is added from non-Federal sources of funds (other than in-kind contributions). These provisions are added by this rule at §210.14(e)(2), (e)(4) and (e)(5).

If a school food authority's average price of a paid lunch is less than the reimbursement difference, the school food authority must increase prices for paid lunches, as described in §210.14(e)(3), or add financial support from non-Federal sources to the school food service account. To determine the price increase, the school food authority must establish an average price for a paid lunch that is not less than the price charged in the previous school year as adjusted by a percentage equal to the sum obtained by adding two percent and the percentage change in the Consumer Price Index for All Urban Consumers (food away from home index) used to increase the Federal reimbursement rate, as set forth in the annual notice announcing adjustments to the national average payments issued by USDA in the Federal Register on or about July 1 of each year. SFAs should refer to the Federal Register notice from the prior July to obtain the Consumer Price Index. For determining increases required for the school year beginning July 1, 2011, SFAs should use the notice published on July 19, 2010 (75 FR 41796, "National School Lunch, Special Milk, and School Breakfast Programs, National Average Payments/Maximum Reimbursement Rates").

Section 205 of the Act amended the NSLA to permit SFAs to round the adjusted average price for a paid lunch down to the nearest five cents following that calculation. Additionally, SFAs are not required to raise prices more than 10 cents annually. SFAs may, at their discretion, increase prices for paid lunches by more than 10 cents. In lieu of increasing prices, a school food authority may reduce the average price of a paid lunch if an equivalent amount of financial support is added from non-Federal sources of funds (other than in-kind contributions). These provisions are found at §210.14(e)(4) and (e)(5).

If a school food authority chooses to contribute financial support from non-Federal sources in lieu of raising prices for paid lunches, Section 12(p) of the NSLA specifically excludes in-

kind contributions and revenue from foods sold in competition with reimbursable meals from qualifying as support from non-Federal sources for this purpose. This rule codifies those prohibitions in §210.14(e)(5)(ii). In addition, §210.14(e)(5)(iii) requires that financial support from non-Federal sources must be cash for direct support for paid lunches, including but not limited to per-lunch reimbursements for paid meals provided by States, counties, school districts and others; funds provided by organizations, such as school-related or community groups to support paid lunches; any portion of State revenue matching funds that exceeds the minimum requirement established in 7 CFR 210.17 and is provided for paid lunches; and a proportion attributable to paid lunches from direct payments made from school district funds to support the lunch service. Some examples of unallowable non-Federal support would include any payments, including additional per-meal reimbursements, provided to the school food authority for support of the SBP or other Child Nutrition Program; any payments, including additional per-meal reimbursements, provided specifically to support free and reduced price meals; and any in-kind contributions converted to direct cash expenditures after July 1, 2011.

In recognition of the short timeframes for implementation, this interim rule allows SFAs to count any non-Federal cash contribution, except for in-kind contributions and revenues from foods sold in competition with reimbursable meals, for School Year 2011-2012 only. This limited allowance is established by this rule in §210.14(e)(6)(iii). In addition, State agencies should focus their efforts in the initial year of implementation to providing SFAs with technical assistance to ensure compliance.

We also recognize that this rule was published after many SFAs have made pricing decisions for School Year 2011-2012. Therefore, those SFAs that can demonstrate that they raised their prices and met the non-Federal cash contribution allowance described above for School Year

2011-2012, may count any non-Federal cash contribution, except for in-kind contributions and revenues from foods sold in competition with reimbursable meals, toward the revenue requirements for School Year 2012-2013. FNS will issue guidance on how adjustments to the School Year 2012-2013 requirement will be determined in these situations.

If an SFA with an average price lower than the reimbursement difference is not required in any school year to increase its average price, due to low-inflation and rounding rules, the school food authority must use the unrounded average price as the basis for calculations for the next school year. This approach helps ensure that over time the appropriate additional revenues are provided to support paid lunches. Also, if a school food authority has an average price lower than the reimbursement difference and chooses in any school year to increase paid lunch prices more than is required, the amount attributable to the SFAs discretionary additional increase may be carried forward to the next school year(s) to meet the paid lunch pricing requirements. SFAs must keep sufficient records to document and carry forward the average price calculations. These requirements are established by this interim rule in §210.14(e)(6)(i) and (e)(6)(ii).

As amended by Section 205 of the Act, Section 12(p) of the NSLA also requires that USDA establish procedures to annually collect and publish the paid meal prices charged by SFAs. While the statute refers to the collection of paid meal prices, this interim rule requires that SFAs report only paid lunch prices. This approach minimizes reporting burden on SFAs and State agencies, and is consistent with the other requirements of Section 205, which all pertain to paid lunches. USDA invites commenters to provide input on whether this approach is appropriate, or whether reporting should be expanded to include prices charged for paid breakfasts. The new reporting requirements for SFAs and State agencies, respectively, are contained in amendments

to §210.15(a) and §210.20(a) made by this rule. This annual report would coincide with other reporting for the month of October.

Revenue from Nonprogram Foods

NSLP regulations are amended by this interim rule to include the new statutory definition of nonprogram food in a new paragraph at §210.14(f). Section 12(p) of the NSLA as amended by the Act defines nonprogram food as "food sold in a participating school other than a reimbursable meal provided" under the NSLA or the Child Nutrition Act of 1966 (42 U.S.C. 1771 et seq.) and which is "purchased using funds from the nonprofit school food service account of the school food authority…." The definition also specifically identifies as nonprogram food "food that is sold in competition with a program established under" the NSLA or the Child Nutrition Act of 1966. Nonprogram beverages are also considered nonprogram food.

Effective July 1, 2011, Section 12(q) of the NSLA, as amended by Section 206 of the Act, requires that the proportion of total school food service revenue provided by the sale of nonprogram foods to the total revenue of the school food service account shall be equal to or greater than the proportion of total food costs associated with obtaining nonprogram foods to the total costs associated with obtaining program and nonprogram foods from the account. The Act also amended the NSLA to require that all revenue from the sale of nonprogram foods accrue to the nonprofit school food service account of a participating SFA. These revenue and accrual requirements are incorporated into NSLP regulations in this interim rule by adding a new paragraph (f) to §210.14.

Technical Amendments

The definition of "Nonprofit school food service account" in §210.2 is revised by adding references to the new procedures in §210.14(e) and (f) regarding revenue. In addition, the requirements in §210.9(b) for the agreement between the State agency and SFAs are amended by adding a reference to these new provisions. Other amendments are made to §210.15(b) and §210.20(b) (for SFAs and State agencies, respectively) to provide for the records that must be retained to document compliance with the newly established provisions in §210.14(e) and (f).

II. Procedural Matters

Issuance of an Interim Rule and Date of Effectiveness

USDA, under the provisions of the Administrative Procedure Act at 5 U.S.C. 553(b)(B), finds for good cause that use of prior notice and comment procedures for issuing this interim rule is impracticable. Sections 205 and 206 of the Healthy, Hunger-Free Kids Act of 2010, Public Law 111-296, enacted on December 13, 2010, requires implementation of those provisions on July 1, 2011. USDA concludes that there is insufficient time to issue a proposed rule prior to the statutory implementation deadline. As a result, this interim rule is necessary to comply with the requirements of Sections 205 and 206 of Public Law 111-296 and ensure that those provisions are implemented and effected by State agencies and SFAs on July 1, 2011.

For the same reason of impracticability due to the statutory implementation deadline, under the provisions of the Congressional Review Act at 5 U.S.C. 808(2), USDA for good cause is issuing this rule with an effective date of July 1, 2011, which is less than the latest of the 60-day delay in effective date prior to, either the submission of a report to Congress, or after publication

of the rule in the Federal Register, as required under section 801(a)(3)(A) of the Congressional Review Act.

USDA invites public comment on this interim rule. USDA will consider amendments to the rule based on comments submitted during the 90-day comment period. The agency will address comments and affirm or amend the interim rule in a final rule.

Executive Order 12866 and Executive Order 13563

Executive Orders 12866 and 13563 direct agencies to assess all costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility.

This interim rule has been designated an "economically significant regulatory action" under section 3(f) of Executive Order 12866. Accordingly, the rule has been reviewed by the Office of Management and Budget.

Regulatory Impact Analysis

As required for all rules that have been designated as significant by the Office of Management and Budget, a Regulatory Impact Analysis (RIA) was developed for this interim rule. It is included as Appendix A at the end of this document.

Regulatory Flexibility Act

This rule has been reviewed with regard to the requirements of the Regulatory Flexibility Act of 1980 (5 U.S.C. 601-612). It has been certified that this rule will have a significant economic impact on a substantial number of small entities. A Regulatory Flexibility Analysis (RFA) was developed for this interim rule and is included as Appendix B at the end of this document.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (UMRA), Public Law 104-4, establishes requirements for Federal agencies to assess the effects of their regulatory actions on State, local, and tribal governments and the private sector. Under section 202 of the UMRA, the Department generally must prepare a written statement, including a cost/benefit analysis, for proposed and final rules with Federal mandates that may result in expenditures to State, local, or tribal governments, in the aggregate, or to the private sector, of $100 million or more in any one year. When such a statement is needed for a rule, section 205 of the UMRA generally requires the Department to identify and consider a reasonable number of regulatory alternatives and adopt the least costly, more cost-effective or least burdensome alternative that achieves the objectives of the rule. This rule does not contain Federal mandates (under the regulatory provisions of Title II of the UMRA) that impose costs on State, local, or tribal governments or to the private sector of $100 million or more in any one year. This rule is, therefore, not subject to the requirements of sections 202 and 205 of the UMRA.

Executive Order 12372

The NSLP is listed in the Catalog of Federal Domestic Assistance under No. 10.555. For the reasons set forth in the final rule in 7 CFR part 3015, Subpart V and related notice (48 FR 29115,

June 24, 1983), this program is included in the scope of Executive Order 12372, which requires intergovernmental consultation with State and local officials.

Executive Order 13132

Executive Order 13132 requires Federal agencies to consider the impact of their regulatory actions on State and local governments. Where such actions have federalism implications, agencies are directed to provide a statement for inclusion in the preamble to the regulations describing the agency's considerations in terms of the three categories called for under section (6)(b)(2)(B) of Executive Order 13132. USDA has considered the impact of this rule on State and local governments and has determined that this rule does not have federalism implications. This rule does not impose substantial or direct compliance costs on State and local governments. Therefore, under Section 6(b) of the Executive Order, a federalism summary impact statement is not required.

Executive Order 12988

This rule has been reviewed under Executive Order 12988, Civil Justice Reform. This rule is intended to have preemptive effect with respect to any State or local laws, regulations or policies which conflict with its provisions or which would otherwise impede its full implementation. This rule is not intended to have retroactive effect unless specified in the DATES section of the final rule. Prior to any judicial challenge to the provisions of this rule or the application of its provisions, all applicable administrative procedures must be exhausted.

Civil Rights Impact Analysis

FNS has reviewed this rule in accordance with Departmental Regulations 4300-4, ”Civil Rights Impact Analysis”, and 1512-1, “Regulatory Decision Making Requirements.” After a careful review of the rule's intent and provisions, FNS has determined that this rule is not intended to limit or reduce in any way the ability of protected classes of individuals to receive benefits on the basis of their race, color, national origin, sex, age or disability nor is it intended to have a differential impact on minority owned or operated business establishments, and woman-owned or operated business establishments that participate in the Child Nutrition Programs.

Paperwork Reduction Act

The Paperwork Reduction Act of 1995 (44 U.S.C. Chap. 35; see 5 CFR part 1320), requires that the Office of Management and Budget (OMB) approve all collections of information by a Federal agency from the public before they can be implemented. Respondents are not required to respond to any collection of information unless it displays a current, valid OMB control number. This is a new collection. The new provisions in this rule, which do increase burden hours, affect information collection requirements that will be merged into the NSLP, OMB Control Number #0584-0006, expiration date 5/31/2012. The current collection burden inventory for the NSLP is 12,257,764. These changes are contingent upon OMB approval under the Paperwork Reduction Act of 1995. When the information collection requirements have been approved, FNS will publish a separate action in the Federal Register announcing OMB’s approval.

Comments on the information collection in this interim rule must be received by [insert 60 days from date of publication in the Federal Register].

Send comments to the Office of Information and Regulatory Affairs, OMB, Attention: Desk Officer for FNS, Washington, D.C. 20503. Please also send a copy of your comments to Lynn Rodgers-Kuperman, Program Analysis and Monitoring Branch, Child Nutrition Division, 3101 Park Center Drive, Alexandria, VA 22302. For further information or for copies of the information collection requirements, please contact Lynn Rodgers-Kuperman at the address indicated above. Comments are invited on: (1) Whether the proposed collection of information is necessary for the proper performance of the Agency's functions, including whether the information will have practical utility; (2) the accuracy of the Agency's estimate of the proposed information collection burden, including the validity of the methodology and assumptions used; (3) ways to enhance the quality, utility and clarity of the information to be collected; and (4) ways to minimize the burden of the collection of information on those who are to respond, including use of appropriate automated, electronic, mechanical, or other technological collection techniques or other forms of information technology.

All responses to this request for comments will be summarized and included in the request for OMB approval. All comments will also become a matter of public record.

Title: National School Lunch Program: School Food Service Account Revenue Amendments Related to the Healthy, Hunger-Free Kids Act of 2010.

OMB Number: 0584-NEW

Expiration Date: Not Yet Determined

Type of Request: New Collection

Abstract:

This interim rule promulgates the provisions from sections 205 and 206 of Public Law

111-296, the Healthy, Hunger-Free Kids Act of 2010 (the Act). Section 205 amended section 12 of the Richard B. Russell National School Lunch Act (NSLA) (42 U.S.C. 1760) by adding a new subsection (p), "Price for a Paid Lunch" which addresses, for the first time, requirements for SFAs on establishing prices for paid reimbursable lunches (hereinafter called paid lunches). Section 205 provided SFAs with some flexibility in phasing-in any increases in paid lunches and in using non-Federal funds to supplement paid lunch revenue in order to keep the price of a paid lunch lower. These provisions do not apply to the revenue from or prices charged for either afterschool snacks or for school breakfasts offered in 7 CFR part 220. There is also a requirement in section 205 requiring USDA to establish procedures to annually collect and publish the paid lunch prices charged by SFAs.

Section 206 of Public Law 111-296 amended section 12 of the NSLA by adding a paragraph (q), "Nonprogram Food Sales." This provision addresses food in schools outside of the reimbursable meal and meal supplements, which are purchased with funds from the nonprofit school food service account. Included are foods sold in competition with these reimbursable meal programs as provided in section 10 of the Child Nutrition Act (42 U.S.C. 1779). The law now requires that the revenue from the sale of nonprogram foods be proportionate to the total revenue generated by such food.

These changes are effective July 1, 2011.

Those respondents participating in the SBP also participate in the NSLP, thus the burden associated with the SBP will be carried in the NSLP. The average reporting and recordkeeping burden per response and the annual burden hours are explained below and summarized in the charts which follow.

Respondents for this Interim Rule: State Agencies (57) and School Food Authorities (20,858)

Estimated Number of Respondents for this Interim Rule: 20,915

Estimated Number of Responses per Respondent for this Interim Rule: 3.991824

Estimated Total Annual Responses: 83,489

Estimated Total Annual Burden on Respondents for this Interim Rule: 322,827

ESTIMATED ANNUAL BURDEN FOR 0584-NEW, NATIONAL SCHOOL LUNCH PROGRAM 7 CFR part 210

Reporting						
	Section	Estimated Number of Respondents	Frequency of Response	Average Annual Responses	Average Burden per Response	Annual Burden Hours
State agency (SA) consolidates paid reimbursable lunch prices reported by SFAs and submits to FNS.	7 CFR 210.14(e)(7)	57	1	57	10	570
SFA reports paid lunch prices for each NSLP school to the SA.	7 CFR 210.14(e)(7)	20,858	1	20,858	0.25	5,215
Total Reporting for Interim Rule		20,915	1	20,915	0.2766	5,785
Total Existing Reporting Burden for 0584-0006, Part 210						2,981,464
Total Reporting Burden Increase with Interim Rule						5,785
Total Reporting Burden for 0584-0006, Part 210 with Interim Rule						2,987,249
Recordkeeping						
	Section	Estimated Number of Respondents	Frequency of Response	Average Annual Responses	Average Burden per Response	Annual Burden Hours
SA maintains records of paid reimbursable lunch prices obtained from SFAs	7 CFR 210.14 (e) (7)	57	366	20,858	0.2	4,172
SFA maintains records of its calculation of the average price of paid reimbursable lunches and adjustments	7 CFR 210.14 (e) (1)-(e)(5)	20,858	1	20,858	5	104,290
SFAs maintains records documenting the revenue generated from the sale of nonprogram foods	7 CFR 210.14 (f)	20,858	1	20,858	10	208,580
Total Recordkeeping for Interim Rule		20,915	2.99	62,574	15.1586	317,042
Total Existing Recordkeeping Burden for 0584-0006, Part 210						9,276,300
Total Recordkeeping Burden for 0584-0006, Part 210 with Interim Rule						9,593,342

SUMMARY OF BURDEN (OMB #0584-NEW)	
TOTAL NO. RESPONDENTS	20,915
AVERAGE NO. RESPONSES PER RESPONDENT	3.991824
TOTAL ANNUAL RESPONSES	83,489
AVERAGE HOURS PER RESPONSE	3.8667
TOTAL BURDEN HOURS FOR PART 210 WITH INTERIM RULE	12,580,591
CURRENT OMB INVENTORY FOR PART 210	12,257,764
DIFFERENCE (NEW BURDEN REQUESTED WITH INTERIM RULE)	322,827

7 CFR 210.15 and 210.20 require that, in order to participate in the NSLP, SFAs and State agencies must maintain records to demonstrate compliance with Program requirements. 7 CFR 210.23 further requires that State agencies and SFAs maintain records for a period of three years.

E-Government Act Compliance

The Food and Nutrition Service is committed to complying with the E-Government Act of 2002, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

Executive Order 13175 - Consultation and Coordination with Indian Tribal Governments

Executive Order 13175 requires Federal agencies to consult and coordinate with tribes on a government-to-government basis on policies that have tribal implications, including regulations, legislative comments or proposed legislation, and other policy statements or actions that have substantial direct effects on one or more Indian tribes, on the relationship between the Federal Government and Indian tribes, or on the distribution of power and responsibilities between the Federal Government and Indian tribes. In spring 2011, USDA engaged in a series of consultative sessions to obtain input by Tribal officials or their designees concerning the impact

of this rule on the tribe or Indian Tribal governments, or whether this rule may preempt Tribal law. Reports from these consultations will be made part of the USDA annual reporting on Tribal Consultation and Collaboration. USDA will respond in a timely and meaningful manner to all Tribal government requests for consultation concerning this rule and will provide additional venues, such as webinars and teleconferences, to periodically host collaborative conversations with Tribal officials or their designees concerning ways to improve this rule in Indian country.

List of Subjects

7 CFR Part 210

Grant programs-education; Grant programs-health; Infants and children; Nutrition; Penalties; Reporting and recordkeeping requirements; School breakfast and lunch programs; Surplus agricultural commodities.

Accordingly, 7 CFR part 210 is amended as follows:

PART 210 – NATIONAL SCHOOL LUNCH PROGRAM

1. The authority citation for 7 CFR part 210 continues to read as follows:

Authority: 42 U.S.C. 1751-1760, 1779.

2. In § 210.2:

a. The definition of "Nonprofit school food service account" is amended by adding a sentence at the end; and

b. The definition of “Subsidized lunch (paid lunch)” is renamed “Paid lunch” and is revised. The addition and revision read as follows:

Subpart A – General

§210.2 Definitions.

* * * * *

Nonprofit school food service account * * * This account shall include, as appropriate, non-Federal funds used to support paid lunches as provided in §210.14(e), and proceeds from nonprogram foods as provided in §210.14(f).

* * * * *

Paid lunch means a lunch served to children who are either not certified for or elect not to receive the free or reduced price benefits offered under part 245 of this chapter. The Department subsidizes each paid lunch with both general cash assistance and donated foods. The prices for paid lunches in a school food authority shall be determined in accordance with §210.14(e).

* * * * *

Subpart C – Requirements for School Food Authority Participation

3. In §210.9, paragraph (b)(1) is revised to read as follows:

§210.9 Agreement with State agency.

* * * * *

(b) Agreement. * * *

(1) Maintain a nonprofit school food service and observe the requirements for and limitations on the use of nonprofit school food service revenues set forth in §210.14 and the limitations on any competitive school food service as set forth in §210.11;

* * * * *

4. In §210.14, new paragraphs (e) and (f) are added to read as follows:

§210.14 Resource management.

*** * * * ***

(e) Pricing paid lunches**.** For each school year beginning July 1, 2011, school food authorities shall establish prices for paid lunches in accordance with this paragraph.

(1) Calculation procedures. Each school food authority shall:

(i) Determine the average price of paid lunches. The average shall be determined based on the total number of paid lunches claimed for the month of October in the previous school year, at each different price charged by the school food authority.

(ii) Calculate the difference between the per meal Federal reimbursement for paid and free lunches received by the school food authority in the previous school year (i.e., the reimbursement difference);

(iii) Compare the average price of a paid lunch under paragraph (e)(1)(i) of this section to the difference between reimbursement rates under paragraph (e)(1)(ii) of this section.

(2) Average paid lunch price is equal to/greater than the reimbursement difference.

When the average paid lunch price from the prior school year is equal to or greater than the difference in reimbursement rates as determined in paragraph (e)(1)(iii) of this section, the school food authority shall establish an average paid lunch price for the current school year that is not less than the difference identified in (e)(1)(iii) of this section; except that, the school food authority may use the procedure in paragraph (e)(4)(ii) of this section when establishing prices of paid lunches.

(3) Average lunch price is lower than the reimbursement difference.

When the average price from the prior school year is lower than the difference in reimbursement rates as determined in paragraph (e)(1)(iii) of this section, the school food authority shall establish an average price for the current school year that is not less than the average price charged in the previous school year as adjusted by a percentage equal to the sum obtained by adding:

(i) 2 percent; and

(ii) The percentage change in the Consumers Price Index for All Urban Consumers used to increase the Federal reimbursement rate under section 11 of the Act for the most recent school year for which data are available. The percentage to be used is found in the annual notice published in the Federal Register announcing the national average payment rates, from the prior year.

(4) Price Adjustments. (i) Maximum required price increase. The maximum annual average price increase required under this paragraph shall not exceed ten cents.

(ii) Rounding of paid lunch prices. Any school food authority may round the adjusted price of the paid lunches down to the nearest five cents.

(iii) Optional price increases. A school food authority may increase the average price by more than ten cents.

(5) Reduction in average price for paid lunches. (i) Any school food authority may reduce the average price of paid lunches as established under this paragraph if the State agency ensures that funds are added to the nonprofit school food service account in accordance with this paragraph. The minimum that must be added is the product of:

(A) The number of paid lunches claimed by the school food authority in the previous school year multiplied by

(B) The amount required under paragraph (e)(3) of this section, as adjusted under paragraph (e)(4) of this section, minus the average price charged.

(ii) Prohibitions. The following shall not be used to reduce the average price charged for paid lunches:

(A) Federal sources of revenue;

(B) Revenue from foods sold in competition with lunches or with breakfasts offered under the School Breakfast Program authorized in 7 CFR part 220. Requirements concerning foods sold in competition with lunches or breakfasts are found in §210.11 and §220.12 of this chapter, respectively;

(C) In-kind contributions;

(D) Any in-kind contributions converted to direct cash expenditures after July 1, 2011; and

(E) Per-meal reimbursements (non-Federal) specifically provided for support of programs other than the school lunch program.

(iii) Allowable non-Federal revenue sources. Any contribution that is for the direct support of paid lunches that is not prohibited under paragraph (e)(5)(ii) of this section may be used as revenue for this purpose. Such contributions include, but are not limited to:

(A) Per-lunch reimbursements for paid lunches provided by State or local governments;

(B) Funds provided by organizations, such as school-related or community groups, to support paid lunches;

(C) Any portion of State revenue matching funds that exceeds the minimum requirement, as provided in §210.17, and is provided for paid lunches; and

(D) A proportion attributable to paid lunches from direct payments made from school district funds to support the lunch service.

(6) Additional considerations. (i) In any given year, if a school food authority with an average price lower than the reimbursement difference is not required by paragraph (e)(4)(ii) of this section to increase its average price for paid lunches, the school food authority shall use the unrounded average price as the basis for calculations to meet paragraph (e)(3) of this section for the next school year.

(ii) If a school food authority that has an average price lower than the reimbursement difference and chooses to increase its average price for paid lunches in any school year more than is required by this section, the amount attributable to the additional voluntary increase may be carried forward to the next school year(s) to meet the requirements of this section.

(iii) For the school year beginning July 1, 2011 only, the limitations for non-Federal contributions in paragraph (e)(5)(iii) of this section do not apply.

(7) Reporting lunch prices. In accordance with guidelines provided by FNS:

(i) School food authorities shall report prices charged for paid lunches to the State agency; and

(ii) State agencies shall report these prices to FNS.

(f) Revenue from nonprogram foods**.** Beginning July 1, 2011, school food authorities shall ensure that the revenue generated from the sale of nonprogram foods complies with the requirements in this paragraph.

(1) Definition of nonprogram foods. For the purposes of this paragraph, nonprogram foods are those foods and beverages:

(i) Sold in a participating school other than reimbursable meals and meal supplements; and

(ii) Purchased using funds from the nonprofit school food service account.

(2) Revenue from nonprogram foods. The proportion of total revenue from the sale of nonprogram foods to total revenue of the school food service account shall be equal to or greater than:

(i) The proportion of total food costs associated with obtaining nonprogram foods to

(ii) The total costs associated with obtaining program and nonprogram foods from the account.

(3) All revenue from the sale of nonprogram foods shall accrue to the nonprofit school food service account of a participating school food authority.

5. In §210.15**:**

a. Amend paragraph (a)(6) by deleting the word "and" at the end of paragraph;

b. Amend paragraph (a)(7) by removing "." at the end of the paragraph and adding "; and" in its place;

c. Add a new paragraph (a)(8);

d. Amend paragraph (b)(5) by removing "." at the end of the paragraph and adding ";" in its place;

e. Add new paragraphs (b)(6) and (b)(7).

The additions read as follows:

§210.15 Reporting and recordkeeping.

(a) * * *

(8) The prices of paid lunches charged by the school food authority.

(b) * * *

(6) Records to document compliance with the requirements in §210.14(e); and

(7) Records to document compliance with the requirements in §210.14(f).

6. In §210.19, paragraph (a)(2) is amended by adding a sentence at the end to read as follows:

Subpart D-Requirements for State Agency Participation

§210.19 Additional responsibilities.

(a) * * *

(2) Assurance of compliance for finances. * * * Each State agency shall ensure that school food authorities comply with the requirements for pricing paid lunches and nonprogram foods as required in §210.14(e) and §210.14(f).

* * * * *

7. In §210. 20:

a. Amend paragraph (a)(7) by deleting the word "and" at the end of paragraph;

b. Amend paragraph (a)(8) by removing "." at the end of paragraph and adding "; and" in its place;

c. Add new paragraph (a)(9);

d. Amend paragraph (b)(11) by deleting the word "and" at the end of paragraph;

e. Amend paragraph (b)(12) by removing "." at the end of paragraph and adding ";" in its place;

f. Add new paragraphs (b)(13) and (b)(14).

The additions read as follows:

§210.20 Reporting and recordkeeping.

(a) * * *

(9) The prices of paid lunches charged by each school food authority.

(b) * * *

(13) Records showing compliance with the requirements in §210.14(e)(5) and records supplied annually by school food authorities showing paid meal prices charged as required by §210.14(e)(6); and

(14) Records to document compliance with the requirements in §210.14(f).

_____ _____

Kevin Concannon
Under Secretary
Food, Nutrition and Consumer Services

Date

Note: This Analysis will not be codified in the Code of Federal Regulations.

Appendix A to 7 CFR 210
Initial Regulatory Impact Analysis

Agency: **Food and Nutrition Service, USDA**

Title: **National School Lunch Program: School Food Service Account Revenue Amendments Related to the Healthy, Hunger-Free Kids Act of 2010**

Nature of Action: Interim Rule

Need for Action: Codifies provisions of Section 205 and 206 of the Healthy, Hunger-Free Kids Act of 2010 in regulation for the National School Lunch Program (NSLP) and the School Breakfast Program (SBP). These provisions set requirements for student payments or other non-Federal revenues to ensure that the paid meals and à la carte foods generate a level of total revenue for local schools that is comparable to the revenue generated by USDA payments for free meals. In the aggregate, these requirements provide additional revenue to support nutritious and healthful meals for all students.

Affected Parties: Those involved in the operation and administration of the NSLP and SBP, including State education agencies, local school food authorities, schools, students, and the food production, distribution and service industry.

Background

The National School Lunch Program (NSLP) is available to over 50 million children each school day; an average of 31.6 million children per day ate a reimbursable lunch in fiscal year (FY) 2010. The School Breakfast Program (SBP) served an average of 11.6 million children daily. Schools that participate in the NSLP and SBP receive Federal reimbursement and USDA Foods (donated commodities) for lunches and breakfasts that meet program requirements.

The level of Federal support provided varies by the household income of the participating child, with the highest payments for meals provided free to the children with incomes below 130 percent of poverty, a lower amount for meals provided at reduced price to those with incomes between 130 percent and 185 percent of poverty, and a small amount for meals provided to higher-income students (paid meals). Recent data on the number of participating students in each category is presented in Table 1.

Table 1: NSLP/SBP Average Daily Participation, FY 2010

Program	Children (millions) Receiving			
	Free Meals	Reduced-Price	Paid Meals	Total

		Meals		
NSLP	17.4	3.0	11.1	31.6
SBP	8.7	1.0	1.9	11.6

While USDA subsidizes paid meals to cover part of the cost of production, local communities and State governments cover the remainder of production costs, and have the flexibility to do so from any non-Federal source – student payments, State subsidies, or local funds. Most schools depend on student payments for paid school meals for a part of their revenue. Based on data collected by USDA from a national sample of schools the full price of lunch for school year 2004-05 was $1.60 on average, and the most common (modal) price was $1.50. The full price ranged from $0.65 to $3.00; on average, it was higher in secondary schools than in elementary schools, and higher in large schools than in smaller ones. The full price was also higher in suburban and lower-poverty schools than in schools not in those categories.[1]

However, the revenue received by schools for paid meals is often too low to cover the cost of those meals. An examination of school meal production costs shows that it cost about $2.28 to produce a school lunch in school year 2005-06.[2] While USDA's reimbursement for a free meal ($2.50), including cash and commodity foods, was about 9 percent higher than reported production costs, total revenues from a paid meal – including the price charged to families ($1.60), USDA's cash reimbursement ($0.21), and the commodity entitlement ($0.175) – was 13 percent less. Total revenue from a paid meal represented only 80 percent of the value of Federal support for a free meal. Funding paid meals below the cost of their production effectively shifts Federal subsidies designed for the lowest-income children to others. It can negatively affect all children by limiting the funds available to provide nutritious meals.

Schools are also authorized to prepare and sell non-program foods and meals during the meal period, as long as the revenue is provided to the food service program account. Revenues from non-reimbursable foods fell short of the cost of producing them by an average of about 29 percent in SY 2005-06.[3] Combining reimbursable meals and other foods, reported costs were essentially equal to revenues (101 percent). The average SFA used revenues from reimbursable meals to offset the cost of producing à la carte and other non-reimbursable food items.

The provisions in Section 205 and 206 of the Healthy, Hunger-Free Kids Act of 2010 set requirements for student payments or other non-Federal revenues to ensure that the paid meals and à la carte foods generate a level of total revenue for local schools that is comparable to the

[1] U.S. Department of Agriculture, Food and Nutrition Service (2007). *School Nutrition Dietary Assessment Study—III* (multiple volumes), Table II.11. (SNDA-III) Report prepared by Mathematica Policy Research. Available at www.fns.usda.gov/ora/.

[2] U.S. Department of Agriculture, Food and Nutrition Service (2008). *School Lunch and Breakfast Cost Study—II* p. ii. (SLBCS-II) Report prepared by Abt Associates, Inc. Available at www.fns.usda.gov/ora/.

[3] *School Lunch and Breakfast Cost Study—II*. The conclusion that schools price à la carte foods below their cost may seem counter intuitive. Some school meal providers may see à la carte food sales as a source of additional revenue for relatively little added cost. Many schools attribute overhead and labor costs primarily to reimbursable meal production and do not recognize that such costs support all meal services, and should be allocated in accordance with generally accepted accounting principles. The research cited here allocates the shared cost of overhead and labor that supports both reimbursable and à la carte meal production proportionately across these services.

revenue generated by USDA payments for free meals. In the aggregate, these requirements provide additional revenue to support nutritious and healthful meals for all students.

I. Summary of Requirements

This interim rule would codify non-discretionary aspects of the following provisions of the Healthy, Hunger-Free Kids Act (Public Law 111-296; the Act) under 7 CFR Part 210:

- Section 205 of the Act requires school food authorities (SFAs) participating in the NSLP to establish a price for paid lunches that is on average equal to the difference between free lunch reimbursement and paid lunch reimbursement – the Section 11 reimbursement.[4] An SFA charging less than the required amount is required to gradually increase the paid lunch price. The maximum annual average required price increase is limited to not more than 10 cents for any SFA. In lieu of increasing the paid lunch price, an SFA may choose to cover the difference in revenue with non-Federal funds. The Act requires the Secretary to develop regulations to carry out this section, including collecting and publishing the prices that SFAs charge for paid meals annually.

- Section 206 of the Act requires that all food sold in a school and purchased with funds from the nonprofit school food service, other than a reimbursable meal provided under the National School Lunch and School Breakfast Programs, must generate revenue at least equal to the cost of such foods.

- The Act makes these provisions effective on July 1, 2011.

II. Cost/Benefit Assessment

A. Summary of Anticipated Impacts

While the rule will have little or no direct impact on Federal expenditures, it will require the contribution of additional funds to the non-profit school meals program account of participating SFAs:

- For the Section 205 provisions, these funds could be derived from a combination of sources, including program participants who receive paid lunches and State and local governments. State agencies administering the NSLP and SFAs have flexibility to determine which of these sources will contribute revenues to meet the requirements, and in what proportion.

[4] Federal reimbursement for NSLP lunches is the sum of the values specified in Section 4 and Section 11 of the Richard B. Russell National School Lunch Act (NSLA). A Section 4 reimbursement is distributed to schools for all program lunches. Lunches served to students eligible for free or reduced-price school meals receive both a Section 4 and a Section 11 reimbursement. SFAs must charge students a price equal to the Federal Section 11 rate (or contribute an equivalent sum from State or local sources) for total per meal revenue from paid meals to match total per meal revenue from free meals. In school year 2010-11, schools earned $2.72 for each free meal, $2.32 for each reduced price meal, and $0.26 for each paid meal.

- For the Section 206 provisions, funds will derive from increased prices for à la carte foods and beverages, and thus will all be contributed by the families of school children who choose to purchase these products.

- School food authorities will be required to incur additional administrative costs to implement the rule, reflecting the need to review food costs and revenue records, adjust à la carte prices, and report the prices charged for paid meals.

In addition, we expect that the rule will have Federal budgetary effects as a result of indirect impacts on participation in the school meals programs. To the extent that the Section 205 provisions result in increased prices for paid meals, NSLP participation may be lower than otherwise projected as students choose not to eat, to bring lunch from home, or to acquire it from other sources, resulting in Federal savings in paid reimbursements. To the extent that price increases for à la carte foods result from Section 206 provisions, school children and their families could choose to substitute reimbursable school meals for purchases of à la carte foods, resulting in increased participation and higher Federal meal reimbursements.

Estimates of the overall impacts of the rule, including both changes in SFA revenues and Federal costs, are presented in Table 2. For purposes of this analysis, the rule is assumed to take effect on July 1, 2011, the start of school year (SY) 2011-2012.

Table 2: Projected Impact of Rule (all figures in millions)

	Fiscal Year					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
SFA Revenues[5]						
Section 205	*	$9	$66	$104	$144	**$323**
Section 206 (non-reimbursable food sales)	175	1,148	1,237	1,320	1,443	**5,324**
Section 206 (reimbursable meal sales)	64	416	466	484	510	**1,939**
Administrative Costs	-5	-9	-10	-10	-10	**-44**
Net SFA Revenues	**$234**	**$1,564**	**$1,760**	**$1,898**	**$2,086**	**$7,542**
Federal Costs						
Section 205 (NSLP)	*	*	-$3	-$7	-$10	**-$20**
Section 206 (NSLP)	46	297	338	348	362	**1,392**
Total Federal Cost	**$46**	**$297**	**$335**	**$342**	**$352**	**$1,372**

[5] SFA revenues derive from increases in student payments for paid lunches and à la carte foods, additional contributions to SFA accounts from State or local governments, and higher USDA reimbursements for an expected increase in participation in the reimbursable meals programs.

Participation Effects						
Net change in number of lunches served	25	155	151	146	143	**620**
Net change in number of reimbursable breakfasts served	**	**	**	**	**	**
Baseline Federal Cost of NSLP	$11,521	$12,049	$12,300	$12,415	$12,534	$60,819
Number of lunches	5,387	5,465	5,531	5,586	5,631	27,600
Baseline Federal Cost of SBP	$3,115	$3,338	$3,470	$3,557	$3,629	$17,108
Number of breakfasts	2,091	2,187	2,253	2,298	2,332	11,160

*** equals less than $500,000.**
**** small increase**

Note: Entries in tables throughout this analysis may not sum to totals due to rounding.

B. SFA Impacts

1. Revenue from Paid Lunches (Section 205)

Section 205 directs SFAs to take steps to equalize the per meal revenue generated by reimbursable paid lunches and free lunches, thus targeting SFAs whose non-Federal per meal revenue is less than the Section 11 reimbursement for lunches (or $2.46 for school year 2011-12). It permits State and local governments to share, or assume fully, the direct economic impact. Although we cannot anticipate how States, local governments, and SFAs will share the responsibility for raising per-meal receipts for paid lunches, we have estimated the total amount of non-Federal revenue needed to meet the requirements compared to the latest observed levels.

We identified schools whose paid meal prices fell short of the Section 11 reimbursement in school year 2004-2005 using data collected in the third School Nutrition Dietary Assessment Study (SNDA-III).[6] This study collected data from a nationally representative sample of 129 SFAs, 398 schools in those SFAs, and 2,314 children attending those schools (and their parents) in School Year 2004-05. SFA directors provided information on district-wide policies (such as menu-planning systems) and operations (such as food purchasing). As part of the study, school foodservice managers provided information regarding their school's foodservice operations, including paid meal prices, and policies on competitive foods available in or near the foodservice area.

To estimate the number of schools that charge less than the Section 11 reimbursement in FY 2011, we assumed that the schools' paid meal prices kept pace with inflation adjustments in the lunch reimbursement since SY 2004-2005. For this analysis, the schools whose prices fall short

[6] Because paid lunch price is a school-level variable on the SNDA-III dataset rather than an SFA-level variable, we perform our analysis at the school level. We developed our estimate as though the responsibility for raising paid lunch prices or finding alternate non-federal revenue rests with individual schools. In practice, Section 205 provides SFAs the flexibility to set prices at individual schools however they see fit, as long as the weighted average price across the SFA meets the Section 205 target. For purposes of an aggregate cost estimate, a school-level analysis and a weighted average SFA-level analysis should give comparable results.

of the Section 11 rate today are the schools that would have fallen short of a comparable regulatory target in SY 2004-2005.[7]

- Throughout the forecast period we assume annual increases in the Section 11 rate equal to the projected growth in the Food Away From Home series of the Consumer Price Index.[8] We also assume that baseline paid meal prices would have matched the annual growth in the Section 11 rate. These baseline prices represent what schools would have charged for reimbursable paid meals in the absence of the interim rule.

- The interim rule requires annual price increases (or equivalent non-Federal revenues) of 2 percent above the inflation rate until prices meet the Section 11 target. The rule also allows for annual rounding of adjusted prices to the next lower 5 cents and limits required price increases to no more than 10 cents. SFAs and schools need not round prices down, nor are they prohibited from imposing annual increases above the 10 cent cap. For this estimate, however, we assume that schools take advantage of both provisions: we assume uniform rounding and no optional price increases above 10 cents in any year.

- The interim rule allows SFAs to contribute financial support from non-Federal sources in lieu of part or all of required paid lunch price increases. It requires that financial support from non-Federal sources must be cash for direct support for paid lunches, and may not be in-kind contributions or revenue from foods sold in competition with reimbursable meals. For the first school year of implementation (school year 2011-12), the interim rule allows SFAs to count any non-Federal cash contribution, except for cash revenues from foods sold in outside of reimbursable meals, as an offset for paid lunch price increases. While the most recent analysis of school meals costs and revenues suggests that State and local authorities contribute substantial non-Federal cash revenues to food service accounts, data is not available to determine the extent to which these revenues represent direct support for paid lunches. For the purpose of this analysis, we assume that SFAs will be able to use existing contributions to meet all of the required paid meal revenue increase to meet the rule's requirements for school year 2011-12, and to meet 25 percent of the requirements for subsequent years.

- We assume that increases in paid meal prices above the 2 percent annual inflation rate reduce student consumption of paid meals.[9] We model this reduction with evidence collected in SNDA-III, which showed that over a range of paid meal prices typical of those charged in SY 2004-2005, student participation rate was lower by 0.11 percent for each additional cent

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[7] It is worth noting that the observed relationship between paid lunch and free lunch revenue is relatively stable across the three SNDA studies, which collected data from school years 1991-92, 1998-99, and 2004-05:

- In SY 1991-92, revenue for a paid meal was 79.9 percent of Federal revenue for a free meal.
- In SY 1998-99, revenue for a paid meal was 80.3 percent of Federal revenue for a free meal.
- In SY 2004-05, revenue for a paid meal was 82.2 percent of Federal revenue for a free meal.

[8] The NSLA provides for annual increases in the Section 11 rate equal to growth in the CPI-U's Food Away From Home series. We use projections in the series prepared by OMB for use in the 2012 President's Budget.

[9] We expect that students that no longer consume paid lunches because of price increases will either bring food from home, choose not to eat during school hours, or acquire food from other sources. We do not have data that allows us to estimate the relative frequency of these different responses.

in paid lunch prices.[10] In addition to impacts on SFA revenues, this participation effect also implies Federal savings; this is discussed further under Federal Budgetary Impacts, below.

The results of this analysis are presented in Table 3:

Table 3: Non-Federal Revenue Required to Meet Paid Meal Revenue Equity Provision

	Fiscal Year (millions)					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Required non-Federal revenue increase based on current estimated paid meal student payments	$8	$56	$87	$138	$192	**$481**
Existing non-Federal, non-student payment contributions that offset required increase	-8	-47	-21	-35	-48	**-158**
Net required non-Federal revenue increase	*****	**$9**	**$66**	**$104**	**$144**	**$323**

Not all school districts will benefit from this revenue increase. We estimate, based on the distribution of paid lunch prices in SY 2004-05 found in SNDA-III, that about 6,000 of 102,000 schools will not have to increase paid meal prices at all in SY 2011-12 to comply with Section 205 because they already charge prices above the $2.46 target for SY 2011-12. An additional 19,000 schools have prices so low (no greater than $1.59) that the 3.14 percent increase required for SY 2011-12 results in an increase of less than 5 cents, and thus in almost all cases rounds down to zero.[11] Almost all of the remaining schools would have only a 5 cent required increase in SY 2011-12.

Because the provision limits the increase to no more than 10 cents per lunch per year, we anticipate that increases in SFAs with the largest difference between paid lunch prices and the Section 11 rate will continue gradually over many years, with about half of all schools reaching the requirements of the rule in 13 years, and many continuing to work towards paid meal revenue parity for 20 years or more.[12]

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[10] Over the price range examined in SNDA-III, this is an elasticity of -0.30. SNDA-I estimated an elasticity of -0.25 over a range of prices from $1.20 to $1.60 in SY 1991-1992. (Table VII.3, p. 137) U.S. Department of Agriculture, Food and Nutrition Service (1993). *The School Nutrition Dietary Assessment Study*. Report prepared by Mathematica Policy Research. Available at www.fns.usda.gov/ora/

[11] These schools would face no required price increase in SY 2011-12 if their SY 2010-11 baseline prices were rounded to an even 5 cent increment. As we note above, this analysis relies on the school-level SNDA-III dataset. Because SNDA-III data indicate that nearly all schools charged prices in 5 cent increments in SY 2004-05, our analysis assumes that all prices in SY 2010-11 are likewise rounded to the nearest 5 cents.

[12] We estimate that the "revenue gap" between free reimbursement and paid meal revenue levels would be reduced 28 percent by FY 2015, the end of the accounting period for this analysis. The gap would continue to shrink in future years.

SFAs have the option of meeting the revenue requirements by adding funds to the school food service account. However, to the extent that SFAs choose instead to raise paid meal prices, the change will affect students (and their families) whose income exceeds the statutory thresholds for free or reduced price meals. While this spares families with the lowest incomes from the revenue raising objective of the provision, there may be some concern that higher paid meal prices will fall disproportionately on children with incomes relatively close to the upper threshold for reduced price benefits. Table 4 presents a distribution of school-aged children by level of family income:[13]

Table 4: Children by Age and Family Income, 2008

Family Income as a Percent of Poverty	Children Age 5-18 Years (000s)	Percent of Total	Percent of Total Ineligible for Free/Reduced Meals
≤ 100%	10,428	18.1%	--
100% to 130%	3,865	6.7	--
130% to 185%	6,686	11.6	--
185% to 200%	1,559	2.7	4.3%
200% to 225%	2,638	4.6	7.2
225% to 250%	2,762	4.8	7.6
250% to 300%	4,988	8.7	13.7
> 300%	24,571	42.7	67.3
Total	57,496	100.0	100.0

The number of school age children with family incomes just over the limit for school meal benefits is substantial in absolute terms; nearly 1.6 million school age children had family incomes between 185 percent and 200 percent of the Federal poverty threshold in 2008. But this group represents roughly 4 percent of all children whose incomes place them among potential paid meal participants.

2. Revenue from Non-Program Foods (Section 206)

a. Direct Impacts on à la Carte Sales

The interim rule requires that, to the extent that SFA revenues from à la carte foods fall short of the rule's cost-based target, SFAs must take positive action to either raise à la carte prices or invest additional sums in program meals.

[13] The data in Table 4 reflect special tabulations of Current Population Survey data prepared by Mathematica Policy Research for FNS.

Required SFA Revenue Increase

We estimate the SFA-level effects of this provision with data collected as part of an examination of school meal production costs (School Lunch and Breakfast Cost Study-II (SLBCS-II)). The SLBCS-II examined school year 2005-2006 revenue and expense data for a nationally representative sample of 120 school food authorities, and a representative sample of 356 schools within those SFAs. Financial statements, meal production records, recipes, invoices, and other documents were reviewed. Data collected from those SFAs include the revenue generated from program meals, the revenue generated from non-program foods that accrued to the school foodservice account, and the cost of producing those meals and food items, allocated between program and non-program foods using generally-accepted accounting practices. Data from interviews with SFA and school district officials were used to calculate unreported costs and allocate labor costs among SFA activities. Samples of meals taken by students were observed to obtain data on menu items sold in reimbursable and nonreimbursable meals.[14]

We use these data to compute the following two key statistics, specified by the rule, for each of the study's sampled SFAs:

Food cost ratio:

$$\frac{\text{cost of non-program foods}}{(\text{cost of program foods} + \text{cost of non-program foods})}$$

Revenue ratio:

$$\frac{\text{non-program revenue}}{(\text{program revenue} + \text{non-program revenue})}$$

Program foods are the Federally reimbursable lunches, breakfasts, and snacks served in the NSLP and SBP. For purposes of the interim rule, non-program foods are à la carte and other items offered to students other than NSLP or SBP meals.[15] As presented in the estimate, the costs for these foods reflect the allocation of food costs across program meals and non-program foods as required under generally accepted accounting principles, including those ingredients and food components that might be purchased and used to support both reimbursable meal service and à la carte service.

The sum of program revenue and non-program revenue in the second ratio is all revenue in the SFA account. SFA revenue includes Federal subsidies for reimbursable meals, USDA food

[14] One limitation of the SLBCS-II for this analysis is that SFAs were not asked to provide separate program and non-program costs. Developing an estimate of the split between program and non-program costs was one of the objectives of the study. Trained observers recorded the foods selected by a sample of students and identified those meals as reimbursable or non-reimbursable. The study then estimated the cost of individual food items based on SFA records of food prices, the value of USDA Foods, school recipe records, and school menus. With this information, the study estimated the share of total food costs attributable to non-program meals. That percentage was applied to non food costs to estimate the overall split between program and non-program costs.

[15] An additional limitation of the SLBCS-II data for this analysis is that financial data for à la carte foods are combined with the data for adult meals, some vending, and catering. Because we cannot isolate à la carte's contribution to these broader measures of cost and revenue we overstate the cost and revenue ratios for some SFAs.

assistance, student payment for program meals, revenue from à la carte and other non-reimbursable food sales, State and local contributions to the SFA account, and a small amount from other sources such as interest on deposits and the sale of equipment.

The interim rule requires SFAs to generate at least as great a share of total revenue from non-program foods as non-program foods contribute to total food costs. That is, SFAs must ensure that their revenue ratio is at least as great as their food cost ratio. With SLBCS-II data, adjusted for growth in student participation and school food prices, we estimate that à la carte revenues fall short of the amount necessary to balance SFA food cost and revenue ratios as required by the interim rule by almost $2.4 billion for the full 2011 fiscal year.[16]

Impacts of Price Changes on Student Purchase of À la Carte Foods

The revenue increase required to balance SFAs' food and revenue ratios for FY 2011 is about 70 percent above projected baseline à la carte receipts.[17] For years beyond 2011, adjustments are needed not only for price inflation, but for changes in demand for à la carte foods as a result of price increases, absent other action by school or SFA administrators.

- In the absence of a direct measure of student sensitivity to price increases in à la carte foods, we use the same price elasticity estimate that we applied to our Section 205 analysis of paid lunches.[18] For each one cent increase in paid meal prices, SNDA-III estimated a -0.11 percent decrease in participation, a price elasticity of about -0.30.[19]

- Following the initial price adjustment to comply with the rule in 2011, we assume that growth in prices charged for and demand for à la carte foods matches growth in the aggregate Federal reimbursement for paid lunches, using the same assumptions for growth in paid lunch participation and reimbursement rates reflected in the FY 2012 President's Budget.[20]

- It is plausible to image that, over time, the effect of increased prices in reducing demand will decay, as consumers grow accustomed to the higher prices. We have not factored this into our analysis, but to the extent that it occurs, we would expect to see demand increase and overall SFA revenue grow.

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[16] For this analysis we assume that baseline demand for à la carte foods grows at a rate comparable to the growth in student consumption of reimbursable paid lunches. We recognize the limitations of paid meal participation as a proxy for à la carte consumption. Our assumption of comparable growth is intended to reflect changes in the size of the student population that chooses to consume school foods but is ineligible for free or reduced price meals.

[17] This is the targeted revenue increase prior to a price-induced drop in demand for à la carte foods.

[18] We find the estimated price elasticity for paid lunches from SNDA-III to be a reasonable substitute for this analysis of à la carte consumption given that it measures student response to price increases in a school setting where available substitutes are comparably limited.

[19] For FY 2011, we estimate that SFAs will need to raise prices to generate $357 million in increased revenue for the period July 1 – September 30. This would require, on average, a 71 percent increase in à la carte prices. We then apply a 3.0 percent reduction in student purchases of à la carte foods for each 10 percent increase in price, estimating that total revenue from à la carte sales will fall by about 21 percent ($182 million). Net SFA revenues thus will increase $175 million, rather than the $357 million that would be raised under an assumption of constant sales.

[20] This means that we assume SFA prices charged for à la carte foods keep pace with increases in the broader market prices of food and labor reflected in the CPI's "food away from home" index.

Through FY 2015, we estimate that SFA revenues for à la carte foods will increase as a result of the interim rule by the amounts in Table 5.

Table 5: Increased SFA Revenue from à la Carte Foods[21]

	Fiscal Year (millions)					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Baseline à la carte revenue	$500	$3,279	$3,533	$3,769	$4,119	**$15,200**
Revenue increase due to price increase	357	2,342	2,524	2,693	2,942	**10,858**
Revenue decrease due to reduced demand	-182	-1,194	-1,286	-1,372	-1,499	**-5,534**
Total adjusted à la carte revenue	675	4,427	4,770	5,090	5,561	**20,524**
Net projected increase in à la carte revenue	**$175**	**$1,148**	**$1,237**	**$1,320**	**$1,443**	**$5,324**

It should be noted that this estimate assumes that the mix of à la carte foods remains equally popular among students relative to price as the foods sold in SY 2004-05 (when the most recent data on à la carte foods was collected), and that schools make no effort to adjust their à la carte offerings to increase their popularity. To the extent that schools make such adjustments, the net revenue increase of the rule would grow.

In addition, the Healthy, Hunger-Free Kids Act of 2010 requires USDA to promulgate nutrition standards for all foods sold in school. Because these standards have not yet been proposed, we did not factor them into this analysis. To the extent that these standards ultimately require schools to eliminate popular items, they could cause a net reduction in demand for à la carte foods, and reduce the revenues generated by this rule.

b. NSLP Participation Impact

We would expect that some portion of the reduced demand for à la carte foods due to price increases would be redirected as additional demand for and participation in the school meals programs.

- We assume that roughly 46 percent of lost demand for à la carte foods due to price increases would be redirected as additional demand for and participation in the school meals programs.[22] For simplicity, and because the consumption of à la carte foods at breakfast is

[21] Reflects a drop in demand following the initial à la carte price increase.

[22] SNDA-III estimates that participation in the reimbursable lunch program is 4.6 percentage points higher in schools that disallow the sale of non-program foods during meal times than in schools that allow non-program food sales (SNDA-III, vol. 2, p. 117). SNDA-I found that 10 percent of students who consumed meals at school purchased their food from à la carte lines, vending machines, or school stores (Table VII.1, p. 131). An overall program participation increase of 4.6 percent from the 10 percent of students who purchase competitive foods

relatively low compared to the consumption of à la carte foods at lunch, we model the shift from à la carte to program foods as one that takes place at lunchtime only.[23] We expect that students that do not choose to participate in school meals or purchase higher-priced à la carte foods will either bring food from home, choose not to eat during school hours, or acquire food from other sources. We do not have data that allows us to estimate the relative frequency of these different responses.

- Data is not available about the income distribution of students who purchase à la carte. We make the assumptions that (1) low-income children are less-frequent consumers of these foods that higher-income children and (2) they are more likely than higher-income children to reduce purchases in response to price increases. We therefore assume that à la carte sales reductions are distributed across school meal eligibility levels in proportion to their share of total program participation.[24]

Our estimate of the increase in SFA revenues that derives from Federal reimbursements and student payments for a larger number of NSLP meals served through FY 2015 as a result of the interim rule is shown in Table 6. This reflects an increase of about 2.9 percent in lunches over the Federal baseline, or about 92 million free lunches, 16 million reduced-price lunches, and 58 million paid lunches in 2015. In addition to impacts on SFA revenues, this participation effect is reflected in increased Federal costs discussed further under Federal Budgetary Impacts, below. (The amounts shown in Table 6 include the Federal costs shown in Table 10, plus additional amounts derived from student payments or other non-Federal revenue sources for non-free meals.)

Table 6: Increased SFA Revenue due to Shift from à la Carte to NSLP Participation

	Fiscal Year (millions)					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Projected increase in SFA revenue from à la carte/NSLP shift	$64	$416	$466	$484	$510	**$1,939**

implies that 46 percent of students who purchase competitive foods will turn to reimbursable meals if competitive food sales are suspended. For this analysis we assume that the percentage increase in program participation by students who stop purchasing competitive foods due to price is the same as the percentage increase in program participation by students whose competitive food option is eliminated entirely.

[23] SNDA-III found that competitive foods were consumed by 29 percent of NSLP non-participants during the lunch period in SY 2004-2005 (Vol. 2, Table VI.9, p. 196), but that competitive foods were consumed by just 5 percent of SBP non-participants during the breakfast period (SNDA-III, Vol. 2, Table VII.9, p. 264).

[24] We assume that 55 percent of children who stop purchasing à la carte foods in response to higher prices are eligible for free school meals, 10 percent are eligible for reduced price meals, and 35 percent are eligible for paid meals. This is the distribution of NSLP participants in FY 2010. If the children who currently purchase à la carte foods are more likely to be eligible for paid meals, estimated revenues would be less than estimated here, especially in the years before the full effect of Section 205 are realized.

3. SFA Administrative Cost

There are no current regulatory requirements regarding pricing of paid lunches, the amount of revenue generated by paid lunches or the revenue generated by selling non-program foods. The interim rule would thus entail new administrative tasks, requiring school food authorities to use information on paid lunch prices, food costs, and revenue records to determine the price changes needed for these meals and à la carte foods.

The rule also requires State agencies and school food authorities to annually provide and report to USDA the paid meal prices charged by school food authorities. We estimate that this will require, in aggregate, roughly 323,000 hours in additional work for States and SFAs each year, increasing administrative costs by about $10 million per year.[25] However, it is important to recognize that, to the extent States and SFAs make use of options to add other non-Federal sources to the school food service account in place of part of all of the price increase, additional administrative costs could result from the need to account for these other revenue sources and amounts. In either case, most additional administrative cost occurs at the SFA level.

Projected administrative costs are shown in Table 7:

Table 7: Administrative Costs

	Fiscal Year (millions)					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Administrative Costs	$5	$9	$10	$10	$10	$44

C. Federal Budgetary Impacts

We estimate that the interim rule has some impacts on Federal expenditures as well. While no measurable direct Federal costs for the implementation of this provision are anticipated, the impact of the pricing and revenue provisions on participation in the NSLP and SBP will change Federal costs for these programs.

To the extent that the Section 205 provisions result in increased prices for paid meals, NSLP participation may be marginally lower than otherwise projected, resulting in Federal savings in paid reimbursements. We model this reduction with SNDA-III data which suggests that the student participation rate was lower by 0.11 percent for each additional cent in paid lunch prices in SY 2004-05. We anticipate that average daily participation by students receiving paid meals will change as a result of this provision as follows:

[25] Based on estimated recordkeeping and reporting requirements for 57 State agencies and nearly 21,000 SFAs. These requirements are expected to impose a burden of about 15 hours per year per respondent (valued at about $30 per hour). We estimate that just half of a full year's worth of these administrative expenses will be incurred in FY 2011.

Table 8: Fewer Children Consuming Paid Meals Due to Higher Prices

	Fiscal Year				
	2011	**2012**	**2013**	**2014**	**2015**
Change in number of children consuming paid meals due to higher prices	*	-7,000	-55,000	-88,000	-124,000

To the extent that price increases for à la carte foods result from Section 206 provisions, this could lead to substitution of NSLP/SBP participation for purchases of these foods, resulting in a marginal participation increase and Federal costs for meal reimbursements. We anticipate that average daily program participation will increase among students switching from à la carte to program meals as a result of this provision as follows:

Table 9: More Children Consuming Program Meals Due to Higher à la Carte Prices

	Fiscal Year				
	2011	**2012**	**2013**	**2014**	**2015**
Children shifting from à la carte to free meals	76,000	482,000	494,000	499,000	509,000
Children shifting from à la carte to reduced price meals	13,000	83,000	85,000	86,000	88,000
Children shifting from à la carte to paid meals	48,000	306,000	313,000	316,000	322,000
Total newly-participating children	**137,000**	**871,000**	**892,000**	**901,000**	**919,000**

The impacts of these effects on Federal expenditures are shown in Table 10.

Table 10: Federal Budgetary Impacts

	Fiscal Year (millions)					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Section 205 – NSLP participation	$0	*	-$3	-$7	-$10	**-$20**
Section 206 – NSLP participation	46	297	338	348	362	**1,392**
Total	**$46**	**$297**	**$335**	**$342**	**$352**	**$1,372**

* Less than $500,000

D. Uncertainties

No regulatory requirements currently exist regarding the prices of paid lunches or non-program foods, and limited data are available to estimate the cost and participation impacts of the interim rule's provisions. Therefore, we made several simplifying assumptions in developing this cost estimate, reflecting gaps in available data and evidence. In this section, we describe the impact of several alternative assumptions on the estimate. The effects of these alternatives on our primary estimates are presented in Table 11.

1. More rapid increase in paid lunch prices

As noted above, Section 205 directs SFAs charging less than the required paid meal price to gradually increase revenue per paid lunch until the requirement is met, with an annual average increase limited to not more than 10 cents. However, schools may choose to raise prices more rapidly than required, and thus generate additional revenue to support their operations.

While our main estimate assumes that schools make only the increases required by the interim rule, Table 11, Section A shows the estimated impact if schools with low paid meal prices raise prices 5 percent above the rate of inflation each year until the requirement is met. This assumption results in an additional $287 million in revenue over five years relative to the main estimate in Table 3.

2. Alternative participation effects increased paid lunch prices

Our main estimate of the participation impact of paid lunch price increases relies on data from SNDA-III, which suggests that over a 50 cent range in paid meal prices (from $1.50 to $2.00 in SY 2004-05) participation was 0.11 percent lower for each one cent increase in price.

We have modeled two alternative assumptions here:

- Table 11, Section B shows the estimated impact if participation decreases at a higher rate – 0.25 percent for each one cent increase in price. This assumption results in a reduction of $160 million in revenue over five years relative to the main estimate in Table 3.

- Table 11, Section C shows the estimated impact if participation decreases at a lower rate – 0.05 percent for each one cent increase in price. This would result in $69 million in additional revenue over five years relative to the main estimate in Table 3.

3. Alternative assumptions for reductions in à la carte food sales

Our main estimate assumes that a 10 percent increase in prices for à la carte foods will reduce purchase and consumption of those foods by 3.0 percent.

Two alternative assumptions about the price elasticity of demand for à la carte foods are presented here:

- Table 11, Section D shows the estimated impact if a 10 percent increase in prices for à la carte food sales relative to food costs reduces purchase and consumption of those foods by 5.0 percent. This assumption results in a reduction of $3.8 billion in revenue over five years relative to the main estimate from Table 5.

- Table 11, Section E shows the estimated impact if a 10 percent increase in prices for à la carte food sales relative to food costs reduces purchase and consumption of those foods by 1.0 percent. This assumption results in $3.7 billion in additional revenue over five years relative to the main estimate from Table 5.

4. Alternative levels of NSLP/SBP participation as a substitution for à la carte sales

Our main estimate assumes that 46 percent of lost demand for à la carte foods due to price increases would be redirected as additional school meals program participation. Two alternative assumptions about this substitution effect are presented:

- Table 11, Section F shows the estimated impact if 20 percent of lost demand was substituted as school meals program participation. This assumption results in a reduction of $787 million in revenue over five years relative to the main estimate in Table 10.

- Table 11, Section G shows the estimated impact if 60 percent of lost demand was substituted as school meals program participation. This assumption results in an increase of $424 million in revenue over five years relative to the main estimate in Table 10.

E. Benefits:

The primary social benefits of the statute as implemented by this interim rule are to ensure that school pricing policies and other non-Federal contributions increase the revenue available to local school food service operations to support production of healthful school meals that are consistent with Federal nutrition standards. It does this by eliminating two unintended Federal subsidies – for paid meals and à la carte foods – that are drawn from payments to support free meals for the lowest-income children. The diversion of these funds negatively affects all children by limiting the funds available to provide nutritious meals.

- USDA's research shows that it cost about $2.28 to produce a school lunch in SY 2005-06.[26] While USDA's reimbursement for a free meal ($2.50), including cash and commodity foods, was about 9 percent higher than reported production costs, total revenues from a paid meal – including the price charged to families ($1.60), USDA's cash reimbursement ($0.21), and the commodity entitlement ($0.175) – was 13 percent less. Total revenue from a paid meal was only 80 percent of the value of Federal support for a free meal.

- Research also shows that revenues in SY 2005-06 from non-reimbursable foods fell short of the cost of producing them by an average of about 29 percent.[27] The average SFA used

[26] SLBCS-II, p. ii
[27] See SLBCS-II

revenues from reimbursable meals to offset the cost of producing à la carte and other non-reimbursable food items.

The provision of additional revenue to the non-profit food service account will provide important financial support to improve the quality of all reimbursable meals. USDA has estimated that the cost of compliance with its proposed rule updating nutrition standards for school meals based on recommendations from the Institute of Medicine (IOM) (RIN 0584-AD59, published January 13, 2011) would increase total costs by roughly 12 percent when fully implemented. The estimated impact of this regulation could increase revenues sufficiently to cover those increased costs,

Table 11: Cost of Rule under Alternate Assumptions

	Fiscal Year					
	2011	**2012**	**2013**	**2014**	**2015**	**Total**
Section A. More Rapid Increase in Paid Lunch Prices						
Net required non-Federal revenue increase	$0	$19	$138	$197	$256	**$610**
Increase Over Primary Estimate	0	10	72	93	112	**287**
Section B. Greater Sensitivity of Paid Meal Participation to Price						
Net required non-Federal revenue increase	$0	$5	$36	$52	$69	**$163**
Decrease From Primary Estimate	0	-4	-30	-51	-76	**-160**
Section C. Lesser Sensitivity of Paid Meal Participation to Price						
Net required non-Federal revenue increase	$0	$11	$79	$126	$177	**$392**
Increase Over Primary Estimate	0	2	13	22	32	**69**
Section D. Greater Price Elasticity of Demand for à la Carte Foods						
SFA à la Carte Revenue	$51	$335	$360	$385	$420	**$1,551**
Decrease From Primary Estimate	-124	-814	-877	-936	-1,022	**-3,773**
Section E. Lesser Price Elasticity of Demand for à la Carte Foods						
SFA à la Carte Revenue	$296	$1,941	$2,091	$2,231	$2,438	**$8,997**
Increase Over Primary Estimate	121	792	854	911	995	**3,673**
Section F. Lesser Substitution of School Meals Participation for à la Carte Sales						

USDA Paid Meal Reimbursements	$20	$129	$147	$151	$158	**$605**
Decrease From Primary Estimate	-26	-168	-191	-197	-205	**-787**
Section G. Greater Substitution of School Meals Participation for à la Carte Sales						
USDA Paid Meal Reimbursements	$59	$388	$441	$454	$473	**$1,816**
Increase Over Primary Estimate	14	91	103	106	110	**424**

support full consistency with existing standards, and ease the path to rapid and full compliance with strengthened nutrition standards, including (1) increased servings of fruits and vegetables, (2) replacement of refined-grain foods with whole-grain rich foods, and (3) replacement of higher-fat dairy products with low-fat varieties.[28] The increased funding to support these meals could not only improve their nutritional quality, but also their appeal to students, leading to further NSLP-SBP participation increases.[29] This in turn would further increase the impact of the proposed standards described above. (It would also increase the SFA revenue and Federal cost that could result from this rule.)

As documented in the IOM recommendations, the proposed changes in school meals standards correspond to inconsistencies between the typical diets of school-aged children in the United States and the *Dietary Guidelines*/*MyPyramid* recommendations. In particular, the report cited an analysis of National Health and Nutrition Examination Survey data for 1999-2002 that showed:

- Total vegetable intake was only about 40 percent of the *MyPyramid* levels, with intake of dark green and orange vegetables less than 20 percent of *MyPyramid* levels.

- Total fruit intake was about 80 percent of the *MyPyramid* levels for children ages 5-8, with far lower levels for older children.

- Intake of whole grains was less than one-quarter of *MyPyramid* levels, although total grain intake was at or above *MyPyramid* levels.

- Intake of dairy products varied by age, with the intakes of the youngest children exceeding *MyPyramid* levels, while those of older children were below those levels. However, most

[28] The regulatory impact analysis for 0584-AD59 estimates the cost of reaching full compliance with improved nutrition standards at $6.8 billion over fiscal years 2012-2016.
[29] The IOM report recommending changes to school meals standards identifies factors in their recommendations that may increase and decrease student acceptance, but also points to efforts in a number of localities in which efforts to improve the nutritional quality of school meals have resulted in increased participation.; See Institute of Medicine (2010). *School Meals: Building Blocks for Healthy Children.* Washington, DC: The National Academies Press, chapter 9, especially pp. 272-275.

dairy consumed contained 2 percent or more milk fat, while the *Dietary Guidelines* recommend fat-free or low-fat dairy products.[30]

The kinds of changes in school meals that this additional revenue will support will promote diets more consistent with the *Guidelines* among program participants. Such diets, in turn, are useful behavioral contributors to health and well-being. As the report of the 2010 Dietary Guidelines Advisory Committee notes, "evidence is accumulating that selecting diets that comply with the Guidelines reduces the risk of chronic disease and promotes health."[31] The report describes and synthesizes the evidence linking diet and different chronic disease risks, including cardiovascular disease and blood pressure, as well as the effects of dietary patterns on total mortality.

Children are a subpopulation of particular focus for the Committee; the report emphasizes the increasing common evidence of chronic disease risk factors, such as glucose intolerance and hypertension, among children, and explains that "[e]vidence documents the importance of optimal nutrition starting during the fetal period through childhood and adolescence because this has a substantial influence on the risk of chronic disease with age."[32]

In response, the report notes improvements in food at schools as a critical strategy to prevent obesity, and related health risks, among children. Indeed, the Committee recommends "[i]mprov[ing] foods sold and served in schools, including school breakfast, lunch, and after-school meals and competitive foods so that they meet the recommendations of the Institute of Medicine and the key findings of the 2010 Dietary Guidelines Advisory Committee. This includes all age groups of children, from preschool through high school."[33]

III. Alternatives

Most aspects of the interim rule are non-discretionary, and tie to explicit, specific requirements of Section 205 and 206 of the Act. Because of the mandatory effective date of July 1, 2011, USDA has chosen to use the plain language of the law to the extent possible and focus exclusively on mandatory requirements in this interim rule. However, the Department made several choices to clarify expectations and requirements for program operators. These are described briefly below.

Section 205: Funding from non-Federal Sources

The law allows SFAs to add "funding from non-Federal sources" in lieu of raising paid meal prices. The law explicitly excludes in-kind contributions and revenue from competitive foods from counting toward a non-Federal contribution, but does not otherwise define the parameters of these contributions. USDA considered the following alternatives defining the scope of allowable funding:

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[30] Institute of Medicine (2010). *School Meals: Building Blocks for Healthy Children.* Washington, DC: The National Academies Press, pp. 49-53.
[31] Dietary Guidelines Advisory Committee (2010). *Report of the Dietary Guidelines Advisory Committee on the Dietary Guidelines for Americans, 2010, to the Secretary of Agriculture and the Secretary of Health and Human Services*. U.S. Department of Agriculture, Agriculture Research Service, Washington, DC, p. B1-2.
[32] Dietary Guidelines Advisory Committee, pp. B1-2, B1-3.
[33] Dietary Guidelines Advisory Committee, p. B3-6.

- *Apart from in-kind contributions and revenue from competitive foods, allow any other cash funding from a non-Federal source to count.* Because funds contributed to the school food service account are provided for a wide variety of purposes, this broad interpretation could result in few, if any, SFAs receiving additional funds that could support the meal service, potentially undermining the intent of this provision.

- *Count only new sources of contributions after July 1, 2011, the effective date of the provision.* This "maintenance of effort" approach would maximize new revenue, but could also penalize SFAs and States that have historically contributed significant non-Federal revenues by requiring them to contribute additional revenue.

- *Allow those non-Federal contributions that provide direct support for paid lunches.* This seemed to cleave most closely to the intent of the law.[34] However, the need to identify and potentially augment such funding sources could be difficult to implement by the July 1 effective date.

The Department chose to allow any non-Federal contribution to the school food service account to count towards the requirement in school Year 2011-12, but for subsequent years to limit contributions to those that are for direct support for paid lunches, in order to balance achieving the intent of the law as soon as possible with enabling implementation in the first year.

Section 205: Calculating the Average Paid Meal Price

To determine the required level of non-Federal revenue, SFAs must calculate the average paid meal price across all paid NSLP lunches served in the district. USDA considered the following alternatives in defining the average price:

- *Average price per lunch*: This method requires SFAs to multiply the number of paid lunches served by the price for each across all schools, add these figures together, and divide by the total number of lunches served in the district for the period. This approach most accurately reflects the total revenue derived from student payments for paid lunches. Because it requires the use of meal counts, it is somewhat more burdensome than the alternative described below.

- *Average price per school):* This would entail SFAs to determine a simple average of prices by school – adding the prices charged at each school and dividing by the total number of schools. This is a simpler calculation, but does not appropriately factor in the number of meals served at each school, or at different price points.

[34] Senate Report 111-178 on the Healthy Hunger Free Kids Act (page 37) notes: "School districts that charge at least the difference between the free lunch reimbursement rate and the paid lunch reimbursement rate for paid meals must adjust their prices on an annual basis by the inflation adjustment factor used for federal reimbursement rates. Participating school food authorities may reduce the average price of a paid lunch required under this section if the State agency ensures that sufficient funding from non-Federal sources (other than in-kind contributions) is *added* to the nonprofit school food service account to compensate for the reduction (emphasis added)."

The Department chose the average price per lunch approach, as it most accurately reflects the payments made by families in support of paid lunches, while requiring only limited additional calculation, and no information that is not readily available to schools and SFAs.

IV. Accounting Statement

Table 12 contains the FY 2011 present values of the figures in Table 2 using a 7 percent discount rate. Table 13 contains present values under an alternate 3 percent discount rate. The rightmost columns of Tables 12 and 13 contain the annualized effects of the rule.

Table 12: Present Value of SFA Revenue and Federal Cost: 7 Percent Discount Rate

	Fiscal Year						
	2011	**2012**	**2013**	**2014**	**2015**	**Total FY 2011-15**	**Annualized Amount**
Transfers (from non-Federal sources to SFA)	$193	$1,193	$1,252	$1,278	$1,331	**$5,247**	**$1,280**
Transfers (from Federal Government to SFA)	46	278	293	279	269	**1,164**	**284**
Costs	5	9	9	8	8	**38**	**9**

Table 13: Present Value of SFA Revenue and Federal Cost: 3 Percent Discount Rate

	Fiscal Year						
	2011	**2012**	**2013**	**2014**	**2015**	**Total FY 2011-15**	**Annualized Amount**
Transfers (from non-Federal sources to SFA)	$193	$1,239	$1,352	$1,433	$1,550	**$5,767**	**$1,259**
Transfers (from Federal Government to SFA)	46	288	316	313	313	**1,276**	**279**
Costs	5	9	9	9	9	**41**	**9**

Note: This Analysis will not be codified in the Code of Federal Regulations.

Appendix B to 7 CFR 210
Initial Regulatory Flexibility Analysis

Initial Regulatory Flexibility Analysis Interim Rule: National School Lunch Program: School Food Service Account Revenue Amendments Related to the Health Hunger-Free Kids Act of 2010
[RIN 0584–AE11]
AGENCY: Food and Nutrition Service, USDA

BACKGROUND: The Regulatory Flexibility Act (RFA) requires agencies to consider the impact of their rules on small entities and to evaluate alternatives that would accomplish the objectives of the rules without unduly burdening small entities when the rules impose a significant economic impact on a substantial number of small entities. Inherent in the RFA is Congress' desire to remove barriers to competition and encourage agencies to consider ways of tailoring regulations to the size of regulated entities.

The RFA does not require that agencies necessarily minimize a rule's impact on small entities if there are significant legal, policy, factual, or other reasons for the rule's having such an impact. The RFA requires only that agencies determine, to the extent feasible, the rule's economic impact on small entities, explore regulatory alternatives for reducing any significant economic impact on a substantial number of such entities, and explain the reasons for their regulatory choices.

Reasons that action is being considered.

Sections 205 and 206 of Public Law 111-296, the Healthy, Hunger-Free Kids Act of 2010 (December 13, 2010), amended the Richard B. Russell National School Lunch Act (NSLA) to address revenue from paid lunches and nonprogram foods (foods and beverages sold by schools outside of the reimbursable meals programs). Beginning July 1, 2011, school food authorities (SFAs) that participate in the National School Lunch Program (NSLP) must assess the prices charged for lunches served to students not eligible for free or reduced prices meals (i.e., paid lunches) and ensure sufficient funds are provided to the nonprofit school food service account in relation to the difference between the higher reimbursement that the Federal government provides for free lunches and the lower reimbursement provided for paid lunches. These funds may come in the form of limited increases in paid lunch prices or by providing additional sources of non-Federal funding to support paid lunches. Section 206 requires SFAs to assure that the proportion of total revenue from the sale of nonprogram foods to the total revenue be equal to or greater than the proportion of total food costs associated with obtaining nonprogram foods to the total costs associated with obtaining program and nonprogram foods from the account.

Objectives of, and legal basis for, the interim rule.

Section 12 of the NSLA was amended by adding paragraphs (p) and (q) which, respectively, address the requirements for revenue from paid reimbursable school lunches and from sale of nonprogram foods. These provisions are intended to ensure sufficient funds are provided to the nonprofit school food service account for meals served to students not eligible for free or reduced price meals and for the cost of obtaining nonprogram foods.

Historically, there have been three main sources of funds provided to nonprofit school food service accounts: Federal reimbursements, paid meal revenues, and State and local funding. Research indicates that average prices charged for paid meals – meals served to students not certified to receive free or reduced price meals – are too low to cover the cost of producing those meals. Pricing paid meals below the cost of their production effectively increases federal subsidies for higher income children at the expense of low income children and negatively affects children across all income levels by limiting the funds available to provide nutritious meals. This same rationale applies to the requirement for assuring that the cost of obtaining nonprogram foods. These provisions will ensure that schools have funding available to support serving nutritious meals to all students

Number of small entities to which the interim rule will apply.

This rule directly regulates the 55 State education agencies and 2 State Departments of Agriculture (SAs) that operate the NSLP and SBP pursuant to agreements with USDA's Food and Nutrition Service (FNS); in turn, its provisions apply to entities that prepare and provide NSLP and SBP meals to students. While SAs are not small entities under the RFA as State populations exceed the 50,000 threshold for a small government jurisdiction, many of the service-providing institutions that work with them to implement the program do meet definitions of small entities:

There are currently about 19,000 School Food Authorities (SFAs) participating in NSLP and SBP. More than 99 percent of these have fewer than 50,000 students.[35] About 26 percent of SFAs with fewer than 50,000 students are private. However, private school SFAs account for only 3 percent of all students in SFAs with enrollments under 50,000.[36]

Nearly 102,000 schools and residential child care institutions participate in the NSLP. These include more than 90,000 public schools, 6,000 private schools, and about 5,000 residential child care institutions (RCCIs).[37] We focus on the impact at the SFA level in this document, rather than the school level, because SFAs are responsible for the administration of the NSLP and the SBP.

Food service management companies (FSMCs) that prepare school meals or menus under contract to SFAs are affected indirectly by the interim rule. Thirteen percent of public school

[35] FNS 742 School Food Verification Survey, School Year 2009-2010. This number is approximate, not all SFAs are required to submit the 742 form.
[36] Ibid. RCCIs include but are not limited to juvenile detention centers, orphanages, and medical institutions. We do not have information on the number of children enrolled in these institutions.
[37] FNS program data for FY 2010.

SFAs contracted with FSMCs in school year (SY) 2004-2005.[38] Of the 2,460 firms categorized as "food service contractors" under NAICS code 72231, 96 percent employ fewer than 500 workers.[39]

Projected reporting, recordkeeping and other compliance requirements.

The analysis below covers only those organizations impacted by the interim rule that were determined to be small entities.

School Food Authorities (SFA)/Schools

- Under the interim rule, school food authorities must ensure that schools that participate in the NSLP generate revenue for paid reimbursable lunches that is comparable to Federal free lunch revenue. Schools must evaluate and gradually adjust the price of paid reimbursable lunches or use non-Federal funding to ensure that the school foodservice account receives sufficient revenue to cover this level.

  To the extent that schools increase prices rather than use other non-Federal revenues to meet the rule's requirements, and these increases reduce demand for paid lunches, NSLP participation could decrease in these schools. However, USDA estimates that this impact will be small – about 0.11 percent for each additional cent in paid lunch prices.

- Under the interim rule, school food authorities must also ensure that revenue from nonprogram foods cover the cost of obtaining those foods. We estimate that this requirement will result in substantial increases in prices charged for nonprogram foods in some schools, and in turn decrease demand for these foods, leading some students to increase consumption of NSLP/SBP meals, and others to acquire food from other sources. (This is described in more detail in Appendix A.

- Finally, the interim rule will require SFAs to report their paid lunch prices to USDA on an annual basis. We have estimated a small increase in reporting burden for SFAs.

While we recognize that these changes may in some cases increase burden on schools and school food authorities, they are explicit requirements of the Healthy, Hunger Free Kids Act of 2010, and will serve the important intent of that law to ensure that schools have funding available to support serving nutritious meals to all students.

Federal rules that may duplicate, overlap or conflict with the interim rule.

FNS is unaware of any such Federal rules or laws.

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[38] U.S. Department of Agriculture, Food and Nutrition Service, Office of Research, Nutrition and Analysis, School Nutrition Dietary Assessment Study-III, Vol. I, 2007, p. 34
http://www.fns.usda.gov/ora/MENU/Published/CNP/FILES/SNDAIII-Vol1.pdf
[39] Ibid.

Significant alternatives.

The law provides for various ways that SFAs can comply with these requirements. The law allows SFAs to limit the increase in the price to a maximum of ten cents annually, although the SFA may choose to raise the price higher. Further, in lieu of a price increase, the SFA may add non-Federal funds to the school food service account in the amount of revenue required to meet the requirement. This interim rule allows SFAs to carry-over any increase above the minimum over subsequent school years. This allows the SFA the flexibility to choose to have price increases only periodically, rather than annually. The law also provides flexibility in establishing how to account for adequate revenue for the cost of obtaining foods sold outside of the school meals programs. Once SFAs determine the proportionate revenue needed for nonprogram foods, it may choose to increase the price of certain items to provide the additional revenue, may do an across the board increase or may choose to add funds from sources outside of the school food service account.